

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968 as amended. Filing is mandatory.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name Harbor-Petoskey Area Airport Authority	County Emmet
Audit Date June 30, 2005	Opinion Date December 20, 2005	Date Accountant Report Submitted to State: January 3, 2005	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

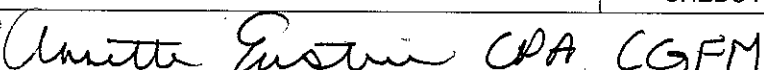
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations.

You must check the applicable box for each item below.

- | | |
|---|---|
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.			X
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).			X

Certified Public Accountant (Firm Name) REHMANN ROBSON ANNETTE EUSTICE, CPA, CGFM			
Street Address 902 SOUTH HURON STREET	City CHEBOYGAN	State MI	Zip 49721
Accountant Signature 			

**HARBOR-PETOSKEY AREA
AIRPORT AUTHORITY**

HARBOR SPRINGS, MICHIGAN

FINANCIAL STATEMENTS

**FOR THE YEAR ENDED
JUNE 30, 2005**

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

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INDEPENDENT AUDITORS' REPORT

December 20, 2005

Members of the Board
Harbor-Petoskey Area Airport Authority
Harbor Springs, Michigan

We have audited the accompanying basic financial statements of the ***Harbor-Petoskey Area Airport Authority*** (the "Authority"), as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2005 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2005, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis on pages I - III is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, reading "Lehmann Lohson". The signature is written in a cursive style with a large, prominent 'L' at the beginning.

Management's Discussion and Analysis

As management of **Harbor-Petoskey Area Airport Authority** (the "Authority"), a non-profit Michigan corporation located in Emmet County, Michigan, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal years ended June 30, 2005 and 2004. Please read it in conjunction with the Authority's financial statements, which immediately follow this section.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements comprise two components: 1) government-wide financial statements (same as fund financial statements) and 2) notes to the financial statements.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The *statement of activities* presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Both of the government-wide financial statements report functions of the Authority that are principally supported by charges for services and member appropriations (*business-type activities*).

Proprietary funds. The Authority is a proprietary fund. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The Authority uses the enterprise fund to account for its airport operations. Proprietary funds provide the same type of information as the government-wide financial statements.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide financial statements. These notes to the financial statements can be found on pages 6-12 of this report.

Government-wide Financial Analysis

Net assets may serve over time as a useful indicator of the Authority's financial position. In the case of the Authority, assets exceeded liabilities by \$684,192 at the close of fiscal 2005.

Approximately 80% of the Authority's net assets reflect its investment in net capital assets. The Authority uses these capital assets to provide services to its customers; consequently, these assets are not available for future spending. The remaining balance of unrestricted net assets (\$138,595) may be used to meet the Authority's ongoing obligations to its creditors.

Harbor-Petoskey Area Airport Authority
Condensed Statement of Net Assets

	<u>2005</u>	<u>2004</u>
Assets		
Current assets	\$ 181,521	\$ 213,149
Capital assets, net of accumulated depreciation	<u>545,597</u>	<u>521,383</u>
Total assets	<u>727,118</u>	<u>734,532</u>
Liabilities		
Current liabilities	<u>42,926</u>	<u>52,087</u>
Net assets		
Invested in capital assets	545,597	521,383
Unrestricted	<u>138,595</u>	<u>161,062</u>
Total net assets	<u>\$ 684,192</u>	<u>\$ 682,445</u>

At June 30, 2005, the Authority was able to report positive balances in both categories of net assets.

Harbor-Petoskey Area Airport Authority
Condensed Statement of Change in Net Assets

	<u>2005</u>	<u>2004</u>
Operating revenues	\$ 566,438	\$ 480,790
Operating expenses	<u>664,785</u>	<u>569,240</u>
Operating loss	(98,347)	(88,450)
Non-operating income	<u>100,094</u>	<u>62,311</u>
Change in net assets	1,747	(26,139)
Net assets, beginning of year	<u>682,445</u>	<u>708,584</u>
Net assets, end of year	<u>\$ 684,192</u>	<u>\$ 682,445</u>

As shown above, the current year operating loss was \$98,347. Operating revenues are directly related to operating expenses. The Authority relies on member appropriations each year from local units of government to help offset costs. The Authority experienced an increase in net assets during fiscal 2005 primarily due to increased member appropriations resulting from the increase from .025 mills to .03 mills assessed and a local contribution to assist in meeting the match requirements of a Michigan Department of Transportation grant.

Capital Assets

At June 30, 2005, the Authority had \$545,597 invested in capital assets. The following table summarizes the capital asset activity for the year:

	Balance July 1, 2004	Additions	Disposals	Balance June 30, 2005
Assets not being depreciated	\$ 47,550	\$ -	\$ (46,430)	\$ 1,120
Assets being depreciated	<u>737,014</u>	<u>111,139</u>	<u>-</u>	<u>848,153</u>
Total capital assets	784,564	111,139	(46,430)	849,273
Less accumulated depreciation	<u>263,181</u>	<u>40,495</u>	<u>-</u>	<u>303,676</u>
Net capital assets	<u>\$ 521,383</u>	<u>\$ 70,644</u>	<u>\$ (46,430)</u>	<u>\$ 545,597</u>

The current year additions to the capital assets were \$64,709 with an additional reclassification of Construction in Progress of \$46,430 to Land Improvements.

Economic Factors

The Authority is a small local airport that relies primarily on fuel sales, various rentals and fees and appropriations from participating local units of government for its support. The participating units include the City of Petoskey, City of Harbor Springs and the Townships of Bear Creek, Little Traverse, West Traverse and Pleasantview. Each municipality pays up to .03 mills on the taxable value of the municipality. In the current year, the Authority levied .03 mills.

The 2005/2006 budget projects continued growth in taxable property values which will result in increased member appropriations. The budget includes expenses similar to the Authority's fiscal 2005 expenses with minimal variations.

Financial Contact

The Authority's financial statements are designed to present users with a general overview of the Authority's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to the Chairman of the Board of Harbor-Petoskey Area Airport Authority, 8479 M-119 Highway, PO Box 274, Conway, MI 49722-0274.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

STATEMENT OF NET ASSETS

JUNE 30, 2005

Assets

Current assets

Cash and cash equivalents	\$ 75,095
Accounts receivable	51,861
Inventory	43,530
Prepaid expenses	<u>11,035</u>

Total current assets **181,521**

Noncurrent assets

Capital assets not being depreciated	1,120
Capital assets, net of depreciation	<u>544,477</u>

Total noncurrent assets **545,597**

Total assets **727,118**

Liabilities

Current liabilities

Accounts payable	40,753
Accrued expenses	<u>2,173</u>

Total liabilities **42,926**

Net assets

Investment in capital assets	545,597
Unrestricted	<u>138,595</u>

Total net assets **\$ 684,192**

The accompanying notes are an integral part of these financial statements.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2005

Operating revenues	
Gasoline and oil sales	\$ 508,587
Hangar rent	16,840
Landing fees	10,358
Tie down and parking fees	9,464
Leases	7,449
Store sales	5,428
Car rental commissions	2,520
Other	5,792
Total operating revenues	566,438
Operating expenses	
Gasoline and oil	364,176
Salaries and wages	98,922
Payroll taxes	14,660
Employee benefits	38,129
Administrative expense	3,253
Maintenance	40,310
Store merchandise	3,222
Equipment rental	449
Insurance	25,772
Professional fees	9,648
Depreciation	40,495
Credit card fees	15,055
Utilities	5,149
Telephone	2,184
Office supplies expense	318
Other expense	3,043
Total operating expenses	664,785
Operating loss	(98,347)
Non-operating revenues	
Local contribution	38,637
Appropriations	57,771
Interest income	3,686
Total non-operating revenues	100,094
Change in net assets	1,747
Net assets, beginning of year	682,445
Net assets, end of year	\$ 684,192

The accompanying notes are an integral part of these financial statements.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2005

Cash flows from operating activities	
Cash collected from customers	\$ 578,445
Cash paid for employee wages and benefits	(98,922)
Cash paid for other operating expenses	<u>(552,887)</u>
Net cash used in operating activities	<u>(73,364)</u>
Cash flows from capital and related financing activities	
Member appropriations	57,771
Local contribution	38,637
Purchase of property and equipment	<u>(64,709)</u>
Net cash provided by capital and related financing activities	<u>31,699</u>
Cash provided by investing activities	
Interest income	<u>3,686</u>
Net decrease in cash and cash equivalents	(37,979)
Cash and cash equivalents, beginning of year	<u>113,074</u>
Cash and cash equivalents, end of year	<u>\$ 75,095</u>
Reconciliation of operating loss to net cash used in operating activities	
Operating loss	\$ (98,347)
Adjustments to reconcile operating loss to net cash used in operating activities	
Depreciation	40,495
Changes in operating assets and liabilities which provided (used) cash	
Accounts receivable	12,007
Inventory	(14,868)
Prepaid expense	(3,490)
Accounts payable	(6,476)
Accrued expenses	<u>(2,685)</u>
Net cash used in operating activities	<u>\$ (73,364)</u>

The accompanying notes are an integral part of these financial statements.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The *Harbor-Petoskey Area Airport Authority* (the “Authority”) is a non-profit Michigan corporation created January 13, 1988 under the authority of Act 206, Michigan Public Acts of 1957, as amended. The purpose of the Authority is to plan, promote, construct, improve, own (or lease), maintain and operate an airport for the benefit of the participating local units of government by providing services to airport users. A board consisting of one member of the following local units of government, all located in Emmet County, Michigan, governs the Authority:

City of Petoskey
City of Harbor Springs
Township of Bear Creek

Township of Little Traverse
Township of West Traverse
Township of Pleasantview

The decision to include a potential component unit in the reporting entity is made by applying the criteria set forth in generally accepted accounting principles. The basic, but not the only, criteria for including an agency, institution, authority or other organization in the governmental unit’s reporting entity is the exercise of oversight responsibility over such agency by the governmental unit’s elected officials. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of the governing authority, the designation of management, the ability to significantly influence operations, and the accountability for fiscal matters. Based on these criteria the reporting entity includes only the Harbor-Petoskey Area Airport Authority.

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standards-setting body for establishing governmental accounting and financial reporting principles.

B. Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on the non-fiduciary activities of the Authority. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. The Authority had no *governmental activities* during the year ended 2005.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

C. Measurement focus, basis of accounting, and financial statement presentation

Government-wide, Proprietary Fund Financial Statements. The proprietary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place.

Proprietary fund operating revenues, such as gas and oil sales, hanger rentals, and other related revenues result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as appropriations and investment earnings, result from nonexchange transactions or ancillary activities.

Nonexchange transactions, in which the Authority gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants and donations. On an accrual basis, revenue is recognized in the financial year for which it is earned. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed for proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Authority has elected not to follow subsequent private-sector guidance.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the proprietary fund's principal ongoing operations. The principal operating revenues of the Authority's proprietary fund are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting that definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

D. Assets, Liabilities and Net Assets or Equity

1. *Deposits*

The Authority's cash and cash equivalents are considered to be demand deposits. State statutes authorize the Authority to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers' acceptances, and mutual funds composed of otherwise legal investments.

2. *Receivables*

All receivables are reported at their gross value net of an estimated allowance for uncollectible accounts, when applicable.

3. *Inventory*

Inventory consists of airplane fuel and other merchandise available for resale, and is reported at the lower of cost or market on a first-in, first-out basis.

4. *Prepaid Expenses*

Prepaid expenses consist of payments made to vendors for services that will benefit future periods. The Authority's prepaid expenses include amounts expended for insurance coverage that extends into the ensuing fiscal period.

5. *Capital Assets*

Capital assets are defined by the Authority as assets that are used in operation and have an initial, individual cost of more than \$1,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

Major outlays for capital assets and improvements are capitalized as projects are purchased or constructed. Capital assets of the Authority are depreciated using the straight-line method over the estimated useful lives as follows:

	<u>Years</u>
Land improvements	20 years
Buildings and improvements	40 years
Other leasehold improvements	20 years
Vehicles	5-7 years
Equipment	5 years

6. *Compensated absences*

Authority employees are not allowed to accumulate sick leave or compensatory time. The Authority has no measurable liability for compensated absences.

7. *Federal Income Taxes*

The Authority is exempt from federal income taxes under Section 115 of the Internal Revenue Code. It qualifies as a non-profit municipal organization formed to maintain an airport on land owned by a municipality, and it serves the general public consistent with Revenue Rule 8-429, 1978-CD 178.

8. *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from those estimates.

2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

The Authority adopts an annual budget each year for expenses applicable to the Proprietary Fund. The operating budget includes proposed expenses and the means of financing them and is stated on a basis consistent with accounting principles generally accepted in the United States of America. Budgets lapse at fiscal year end.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

3. DETAILED NOTES ON ALL FUNDS

A. Deposits

Deposit balances as of June 30, 2005 consisted of cash and cash equivalents of \$75,095. Custodial risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned. State law does not require and the Authority does not have a policy for deposit custodial risk. As of year end, \$20,073 of the Authority's bank balance of \$120,073 was exposed to custodial credit risk because it was uninsured and uncollateralized.

The Authority believes that due to the dollar amount of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Authority evaluates each financial institution with which it deposits Authority funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

B. Capital Assets

Capital assets activity was as follows for the year ended June 30, 2005:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets not being depreciated				
Land	\$ 1,120	\$ -	\$ -	\$ 1,120
Construction in progress	<u>46,430</u>	<u>-</u>	<u>(46,430)</u>	<u>-</u>
Total capital assets not being depreciated	<u>47,550</u>	<u>-</u>	<u>(46,430)</u>	<u>1,120</u>
Capital assets being depreciated				
Land improvements	543,915	97,815	-	641,730
Buildings and improvements	61,694	-	-	61,694
Other leasehold improvements	59,535	-	-	59,535
Vehicles	52,826	11,542	-	64,368
Equipment	<u>19,044</u>	<u>1,782</u>	<u>-</u>	<u>20,826</u>
Total capital assets being depreciated	<u>737,014</u>	<u>111,139</u>	<u>-</u>	<u>848,153</u>

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Accumulated depreciation				
Land improvements	\$ (165,857)	\$ (29,990)	\$ -	\$ (195,847)
Buildings and improvements	(13,601)	(1,554)	-	(15,155)
Other leasehold improvements	(32,203)	(2,861)	-	(35,064)
Vehicles	(33,756)	(5,186)	-	(38,942)
Equipment	(17,764)	(904)	-	(18,668)
Total accumulated depreciation	<u>(263,181)</u>	<u>(40,495)</u>	<u>-</u>	<u>(303,676)</u>
Total capital assets being depreciated, net	<u>473,833</u>	<u>70,644</u>	<u>-</u>	<u>544,477</u>
Capital assets, net	<u>\$ 521,383</u>	<u>\$ 70,644</u>	<u>\$ (46,430)</u>	<u>\$ 545,597</u>

4. OTHER INFORMATION

A. Leases

Hanger Rentals – The Authority, as part of its normal operating procedures, leases airplane storage to airport users. Leases are entered into on an annual basis with rents being paid monthly. Hanger rental revenue generated during the year ended June 30, 2005 was \$16,840.

Other Leases – The Authority receives certain revenues derived from the lease of land. Under the provisions of these leases, the tenants were permitted to construct or maintain facilities restricted for their exclusive use which are separate and apart from normal airport facilities. Revenue generated during the fiscal year ended June 30, 2005 was \$7,449. The Authority is not committed to maintain facilities or expend funds under these lease arrangements.

The Authority leases airport facilities including land, buildings and certain equipment from the City of Harbor Springs (\$1 per year). The lease is for 25 years and automatically renews each year for an extension of one year. The lease obligates the Authority to operate and maintain the airport in conformance with federal and state guidelines and regulations, and to promote and develop the airport for the benefit of the community. Either party can opt to not extend the lease beyond the 25 years; however, the Authority anticipates the lease will be renewed annually.

HARBOR-PETOSKEY AREA AIRPORT AUTHORITY

NOTES TO FINANCIAL STATEMENTS

B. Risk management

The Authority is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters for which it obtains coverage from commercial insurance companies. The Authority has had no settled claims resulting from these risks that exceeded their commercial coverage in any of the past three fiscal years.

C. Other matters

In August 2004, the Authority signed a contract with the Michigan Department of Transportation for a taxiway and lighting project. The estimated cost is \$579,300. State grants will pay \$483,155 of the cost and the remaining \$96,185 is to be paid by the Authority. As of June 30, 2005, the Authority had expended its local match. Approximately \$39,000 of the Authority's share was paid by a local third party who will benefit from the project at the airport.

* * * * *



INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

December 20, 2005

Board of Directors
Harbor-Petoskey Area Airport Authority
Harbor Springs, Michigan

We have audited the basic financial statements of the *Harbor-Petoskey Area Airport Authority* (the "Authority") as of and for the year ended June 30, 2005 and have issued our report thereon dated December 20, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, others within the Authority, and the Authority's Board of Directors and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style.